

# Weekly Market Focus

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HINDUJA BANK  
SWITZERLAND

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## ASSET CLASS REVIEW

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While the euro may strengthen further over the short term, we keep on thinking that equities in the Eurozone should continue to outperform the US ones, where the economy is more mature.

### Eurozone Equities

In principle, a stronger currency can weigh on equities by reducing the local-currency value of overseas earnings of multinationals, and by worsening the outlook for exports. The Nikkei 225 for example, tends to fall as the yen appreciates, and vice versa.

However, euro-zone equities do not appear to have been much perturbed by the euro's recent strength. The single currency has risen by 7% against the dollar this year, making it the best performing G10 currency, and yet the Euro-Stoxx index has risen by over 10% in local currency terms. What's more, the rally has been broad-based, with German, French, Italian and Spanish equities all rising by over 8%.

This does not surprise us. Euro-zone equities have often moved in the same direction as the euro. They both rose in the early 2000s, while both fell in the aftermath of the financial crisis.

The two often move together because the outlook for growth and/or the risk of euro-zone break-up act as the common dominant drivers. Recently, the outlook for growth has improved considerably, while Emmanuel Macron's victory has also allayed investors' worst fears of a trend towards populism.

The rise in the PMI over the past 10 months reflects the improved economic backdrop, and has coincided with a surge in equities. This has encouraged large inflows into bonds and equities, primarily from the US, which in turn have caused the euro to appreciate.

Analysts forecast strong euro-zone GDP growth this year and next, supported by continued exceptionally loose ECB policy. Indeed, we expect rates to remain on hold until 2019. In the meantime, wage growth is likely to remain subdued, unlike in the US, so there is scope for earnings to grow further. However, euro-zone political risk has by no means disappeared and could flare up again in Italy before long.

On balance, though, one should expect equities in the euro-zone to outperform those in the US.

We see the S&P 500 moving sideways until the end of next year, but forecast the DAX to rise further from the present level to around 13,500 by year-end.

## FOREX

### Overview

The Dollar has again lost ground in line with stocks while bonds and safe haven assets gain amid poor risk sentiment and geopolitical concerns. The JPY has appreciated to its strongest level 109.28 since April. Gold and Treasuries too rose following the weaker NFP data on Friday and again following the terror attacks in London. Markets have turned cautious following a seven-week surge for global stocks. Safe haven assets are in favour, with US 10-year Treasury yield trading on at levels not seen since November at 2.15%. NFP did little to dent expectations on the future Fed interest rate path with a 90% probability discounted into the curve. This week sees key central banks meeting on monetary policy, notably the ECB. Attention this week also focuses on the UK election. The ECB releases its policy decision Thursday. Mario Draghi is not expected by the majority to adjust policy however the bank may drop the reference to “downside” risks to growth, while reiterating a weak inflation outlook. The election in the UK this week reflect a tighter race than originally thought increasing the chance the PM May might not bolster her majority. Finally, there may be some attention on the testimony from former FBI head James Comey on Thursday.

### EUR

The ECB is expected to upgrade its economic assessment this Thursday leading to possible changes to the forward guidance. The markets were disappointed last week with the release of the May inflation report which showed the jump in the April core data been mostly due to Easter effects, causing a minor dip in the Euro spot price. We see the ECB will be reluctant to shift too far from its current dovish stance considering recent rhetoric from Draghi which may result in further Euro weakness. We have been bearish while prices remain below the 1.1300 ceiling however the consistency of Euro bulls currently questions this view, and future dips will be shallow. Despite hawkish sounds from a minority on the GC we agree with market consensus that the majority will chose for only small change to the language, with the removal of the word ‘or lower’ when referring to key ECB interest rates. Draghi is also expected to refer to the Eurozone economy as being balanced. Technically EURUSD has seen a large divergence of the daily RSI just ahead of the 1.1300 November high, which reflects a loss of upside momentum. The Euro is well placed to test the 1.1300 November 2016 high, however we suspect that this may hold considering the above points. Any dip in the common currency will be met with good supply, with strong support seen at the near term uptrend at 1.1075. Near term support is at 1.1216. Above 1.1300, the market has potential to reach the highs from mid-2016 circa 1.1429 and the two year resistance line at 1.1474, however we believe it will struggle here from a longer term perspective. There is strong Fibonacci resistance at the 78.6% line, 1.1343 in price. There are some warning signals apart from divergence. The EU-US 10Y swap spread has reached the 50% retracement at -1.324bps and we note the 13 count on the daily chart. This signals exhaustion to the FX price. Last week we recommended being short EURUSD in the near term at 1.1260/70 area with stops just above 1.1300. On a medium term basis we still favour being long Euro on dips towards 1.1100. EURGBP too has divergence on the daily RSI, pointing to failure at the top of its 6 month range. Here we recommended selling at the 0.8750 resistance area which has capped attempts to trade higher lately. We see potential for dips back towards the 200 day and 55 day ma at .8605/15. EURGBP has the potential to move the most this week on a dovish ECB and Tory majority in the UK.

**GBP**

The UK holds the snap election this Thursday. Recent polls indicate that the race is closer than originally thought raising the uncertainty of the result. How will the pound react in the aftermath of the results?

Originally when PM May called for an election the pound gained. The market assumed that it would be a landslide victory as the Tories led Labour Party by 20 percentage points. This would therefore allow the Tory party to gain a large majority in parliament to push through policies resulting in a smooth Brexit. However, this lead has narrowed considerably since, and according to some polls the Tories might even lose their majority in Parliament.

There are three scenarios unfolding:

1. The Tories win and maintain their majority in Parliament or even increase it further.
2. Labour wins a majority in Parliament.
3. Neither Labour nor the Tories gain a majority.

1. In this scenario, we can assume that Sterling is likely to appreciate. That would be consistent with the market reaction over the past weeks. A clear Tory victory would give May an almost free hand in the negotiations with the EU. She would be able to impose her Brexit strategy.

2. Should Labour win, Sterling is likely to depreciate due to a higher uncertainty regarding Brexit. Sterling has weakened since Labour started gaining ground in the polls. This weakness however is likely to be short lived as the likelihood of a hard Brexit in case of a clear Labour victory would be reduced. Labour is not planning to revoke Brexit and Labour leader Jeremy Corbyn currently is committed to continue negotiations with the EU.

3. Lastly, and what would be troublesome for the pound is that no party obtains a majority, possibly resulting in a coalition government. The formation of a new government takes time further delaying talks with the EU.

Recently we suggested buying a downside Seagull structure as a protection to sterling weakness. We see sterling strengthening from here and recommend shorting EURGBP at 0.8750/60 with a stop just above the recent high at 0.8775/80. Downside targets rest at 0.8610 (200mda).

**USD/CHF**

USDCHF has continued its path lower and currently tests the two year trend line from May 2015 at and around 0.9650. Momentum is stalling and there are signs of a base being formed on shorter duration charts. Fibonacci and wedge pattern extensions indicate that prices could further deteriorate to 0.9550 the 200 moving week average and the low for 2016. Resistance to the upside is first found at 0.9715/20 and above at 0.9800/15. Above there the 200 mda should cap any assault over the medium term at 0.9970.

**JPY**

USDJPY has suffered recently in the wake poor risk sentiment. Lower US long term rates, heightened geopolitical risks, concerns over long term inflation expectations and disappointing US economic data all contributing factors. Prices have seen the weakness extend to ultimate support levels at 109.23.

We see a further decline in USDJPY unlikely from here and favour being long at this juncture. US 10yr yields are currently supported from a long term trend line from July 2016. There currently is nothing to suggest that Fed will not increase rates in June, and again later this year bringing the Fed Funds Rate to 1.50%. Interestingly on the charts we have now just closed a gap on the 10 year yield from the US election result in Nov 2016.

Buy USDJPY at 109.20/35, stop at 108.90 (close), targeting 110.40.

## VIEWS FROM THE TRADING FLOOR

### Equity

S&P was up 0.7% on the last week, with no change in volatility, VIX moving from 10.45 to 10.38. On the upside we have tires & rubber up nearly 8% and health care suppliers up 5%. On the down side we only have department stores down 7%..

In the US, without significant macro-economic data, the focus this week will be on the former FBI director James Comey's testimony. On Thursday, the latter will testify in public session before the Senate committee of inquiry on the Russia affair. Allegedly, he will thereby confirm that US President Trump pressured him to terminate his investigations against former security advisor Michael Flynn. If this was confirmed, the US President should come under even greater pressure.

S&P 500: The index is still struggling but continues its rise toward the first target area 2484-2500. The next one being 2600.

On the downside 2370 remains the first support before 2350 and 2325, below this level 2300 is the most probable target of any downward move.

Eurostoxx 50: The index has not managed to regain momentum and move above 3600. It is currently moving in a broad trading range between 3525 and 3600.

A new break above 3600 will lead to a test of the recent high at 3666 before 3700 and a potential extension toward 3836.

The first strong support remains 3525 (with an intermediate one at 3550) any close below this level will lead to a test of 3450 support.

### EQUITY

#### Developed countries

##### Total return - 1 Week

SMI	↓	-0.4%
Euro Stoxx 50	↓	-0.2%
DAX	↓	-0.1%
FTSE 100	↑	1.8%
S&P 500	↑	0.1%
Dow Jones	↑	0.3%
Nikkei 225	↓	-0.4%

#### Developing countries

Russia/Micex	↓	-1.5%
India/Nifty 50	↑	1.3%
China (HK)	↑	1.4%

↑ - Upward move      ↓ - Downward move

### FIXED INCOME

#### Developed countries

	2-year Yield	10-year Yield
USA	1.3%	2.3%
UK	0.1%	1.1%
Germany	-0.7%	0.4%
France	-0.4%	0.8%
Italy	-0.3%	2.2%
Spain	-0.3%	1.6%
Switzerland	-0.9%	-0.1%

#### Developing countries

	2-year Yield	10-year Yield
Russia	2.0%	4.0%

### COMMODITIES

##### Total return - 1 Week

Crude Oil	↓	-7.2%
Gold	↓	-3.0%



## CALENDARS

### Economic Events

Date of release	Domicile	Event	Period	Actual	Estimated
08 June 2017	JN	GDP SA QoQ	1Q F	0.60%	0.50%
08 June 2017	EC	ECB Main Refinancing Rate	08 June 2017	0.00%	0.00%
08 June 2017	US	Initial Jobless Claims	03 June 2017	240k	248k
09 June 2017	CH	CPI YoY	May	1.50%	1.20%
09 June 2017	FR	Industrial Production MoM	Apr	0.20%	2.00%
14 June 2017	US	CPI MoM	May	0.00%	0.20%

### Company Earnings

Date of release	Domicile	Company Name	Period	Estimate EPS
14 June 2017	SP	Industria de Diseno Textil SA	Q1 18	0.21

## Contacts

### Geneva – Headquarters

#### Hinduja Bank (Switzerland) Ltd

Place de la Fusterie 3bis  
1204 Geneva, Switzerland  
Tel. +41 58 906 08 08  
Fax +41 58 906 08 00

### Branches

#### Zurich

Florastrasse 7  
8008 Zurich, Switzerland  
Tel. +41 58 906 05 05  
Fax +41 58 906 05 06

#### Lugano

Viale Serafino Balestra 5  
6900 Lugano, Switzerland  
Tel. +41 91 910 43 43  
Fax +41 91 923 55 73

### Representative Offices

#### London

Amas Investment &  
Project Services Ltd  
Room no: 117,  
First Floor, Regus,  
100 Pall Mall,  
London SW1Y5NQ  
Tel. +44 20 7321 5642

#### Paris

Rue Galilée 33  
75116 Paris, France  
Tel. +33 1 44 43 52 36  
Fax +33 1 40 70 03 79

### Subsidiaries

#### Switzerland

Berafina AG  
Münchensteinerstrasse 43  
4001 Basle, Switzerland  
Tel. +41 61 225 45 45  
Fax +41 61 225 45 25

#### Rowena AG

Grenzstrasse 24  
9430 St Margrethen, Switzerland  
Tel. +41 71 747 49 59  
Fax +41 71 747 49 51

#### Dubai

Hinduja Bank (Middle East) Ltd  
Dubai International Financial Centre  
Building GV 10, 2nd Floor, Unit 5  
Dubai, UAE 506783  
Tel. +97 14 436 65 88

#### Mauritius

Hinduja India Mauritius Holdings Ltd  
HBS Trust Services (Mauritius) Ltd  
1st Floor, Manor House Cr. St. James  
Chazal Street Port Louis, Mauritius  
Tel. +230 208 75 75  
Fax +230 208 75 74

#### USA

Hinduja Capital Advisors Inc  
520 Madison Ave., 34th Floor  
New York, 10022, USA  
Tel. +1 212 355 07 55  
Fax +1 212 752 73 12

#### UK

Amas Investment & Project Services Ltd  
New Zealand House  
Haymarket 80  
London, SW1Y 4TE, United Kingdom  
Tel. +44 20 7839 4661  
Fax +44 20 7839 5992

#### India

Paterson Securities Pvt Ltd  
Bhavani Mansion 3, 4th Lane  
Nungambakkam High Road  
Chennai - 34  
India

#### Cayman Island

Hinduja Bank & Trust (Cayman) Ltd  
c/o P.O. Box 2407GT  
Grand Cayman  
Cayman Islands

## Publisher

### Hinduja Bank (Switzerland) Ltd

Place de la Fusterie 3 bis

1204 Geneva, Switzerland

Tel. +41 22 906 08 08

Fax +41 22 906 08 00

[www.hindujabank.com](http://www.hindujabank.com)

[info@hindujabank.com](mailto:info@hindujabank.com)



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